

Bureau for Development Policy

*MAKING SENSE OF MDG COSTING**

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Abstract

MDG costing is necessary for integrating global development goals into national poverty reduction strategies. But the price tag of the MDGs depends on strategic choices about the ways and means for reaching the targets. Since the technical experts seldom agree on the optimal path towards the MDGs, it is best to approach MDG costing through a participatory process of political economy, driven by tailored targets for 2015 that are expressed in intermediate targets and actionable propositions. When estimating MDG costs, the key words must be flexibility, humility and learning. None of the existing methods yield robust or accurate cost estimates. In making sense of MDG costing, more attention must be paid to country-level estimates than to global ones; to the short-to-medium time horizon than to the long-term one; to relative cost estimates than to absolute ones; to domestic sources of funding than to foreign aid; and to national ownership than to donorship. Three practical steps are proposed for aligning the PRSP and the MTEF with MDG targets in a meaningful way. They are based on the premise that for the sake of the MDGs, prudence is silver but ambition is golden.

“There is an evil in extreme impatience as well as in extreme patience with social ills.”
 Alfred Marshall, *Principles of Economics*, 1890

1. Global targets, local progress

The millennium development goals (MDGs) stipulate quantitative reductions in the various dimensions of human poverty by 2015, ranging from hunger, disease and ignorance to gender discrimination and environmental degradation.

By and large, the numerical targets were set on the premise that the progress observed in the 1970s and 1980s at the global level would continue over the lifetime of one generation – covering the 25 years between 1990 and 2015. Were such progress to be maintained for child survival, for instance, the average under-five mortality rate in developing countries would be reduced by two-thirds between 1990 and 2015. While this target is valid at the global level, it is not necessarily so for each and every country.

Global targets are valid but not all nations can meet them because country-specific circumstances differ significantly from global trends. The Philippines, for instance, is closer to reflecting the global trends than, say, Chad is. Countries that face an acute HIV pandemic cannot be expected to achieve the same progress in human development than countries that do not face such a challenge.

Target setting at the national level is more about adaptation than about adoption. The spirit of the Millennium Declaration is not to impose a uniform set of targets on each and every country. The MDG targets must be tailored and customised to reflect national circumstances and priorities. In describing his country’s recent progress towards universal primary education, Tanzania’s President stated, “I am now convinced that the MDGs can only be attained through a global compact, anchored in national policies that take into account local circumstances” [International Herald Tribune, 13 July 2004].

Setting country-specific targets does not mean that the global targets will be abandoned or watered down. The global targets will not be undermined if some countries set lower national targets because others will set targets that exceed the global ones – so-called ‘MDG-plus’ targets. In the aggregate, global targets will still be met because global progress is an average of country-specific performances.

The global trends on which the MDG targets are based are, after all, the result of aggregating millions of very different trends across individuals, families, communities and countries. National development planning and target setting cannot be driven by such aggregations and abstractions. Global targets abstract away a country’s history, deep-seated social and gender disparities and other specific challenges. Global targets cannot be interpreted as one-size-fits-all objectives; the Millennium Declaration does not assume homogeneity across national borders.

Moreover, the imposition of global targets inherently undermines national ownership, which remains weak in several countries. Creating the space to tailor the MDG targets is essential for generating a stronger sense of ownership among national stakeholders.

At the same time, tailoring national targets cannot become an euphemism for abandoning the political commitment made at the Millennium Summit to “spare no effort to free our fellow men, women and children from the abject and dehumanising conditions of extreme poverty” [Millennium Declaration, 2000]. Setting country-specific targets that lack in ambition and in urgency would be an escape clause from that commitment.

Thus, the focus must gradually shift from global targets to local progress. The efforts to set region-specific targets in South Asia is a step in that direction. Global targets need to be complemented by tailored and customised targets at the national and sub-national levels as benchmarks for success. The question is not whether a country or a community is on track vis-à-vis the global targets; it is whether the greatest and fastest possible progress is being made – given the specific constraints faced by that country or community and given the level of external support. It is not about being on track globally but about accelerating progress locally.

2. Power of quantification

The MDGs have moved quickly to the centre of the international development agenda, in large part due to the power of quantification. For the first time, we have an internationally agreed agenda for human development that can be monitored in quantitative terms. Estimating the financial cost of operationalising the MDG agenda is driven by that same power. Sayings such as ‘if it cannot be measured, it cannot be managed’ and ‘if it cannot be counted, it does not count’ are popular expressions of the power of quantification. Social science increasingly adopts the motto that ‘nothing can be known unless it can be quantified’.

Several attempts are underway to estimate the cost of achieving the MDGs – at the global level and in several countries, as well as sectorally. One of the first estimates was made by the Zedillo Commission in preparation of the international conference on Finance for Development in 2002. It estimated that realising the MDGs at the global level would require at least an extra \$50 billion per year.

Attempts to quantify the cost of realising the MDG agenda use very different methods. Not only do they calculate the cost of operational interventions differently, they handle issues of absorptive capacity, ‘good’ policies and the Dutch disease in various degrees of detail. A review of these methods and approaches shows that MDG costing is not an exact science. None of the existing cost estimates is robust to the assumptions made – however plausible they may be. Each methodology seems to be driven by an implicit agenda – either to make the case for more aid, to caution vis-à-vis absorptive capacity or to promote ‘good’ policies.

Notwithstanding the imperfect methodologies, the importance of MDG costing is beyond doubt. MDG costing provides a quantitative basis for defining anti-poverty strategies and programmes, as well as for forecasting needs and gaps and for mobilising additional resources. But the methodologies that underpin such attempts have severe limitations. By

reviewing them in some detail, we do not imply that MDG costing is a futile exercise. The question is not whether to attempt MDG costing or not; it is how best to do it and for what purpose. Cost estimates have been valuable for the purpose of advocacy vis-à-vis pro-poor budgeting and more foreign aid.

3. Methodological issues

As the targets themselves, the relevance of MDG costing lies mainly at the national and sub-national levels. The primary purpose of estimating the price tag of the MDGs is to align the national budget, sectoral plans and foreign aid with the country-specific targets. Flexibility is crucial because MDG costing must be premised on two basic and inter-related assertions, namely that:

- (i) it cannot be known in advance with any reasonable degree of certainty how the MDGs will be achieved in a particular country or community; and
- (ii) it cannot be known in advance with any sensible degree of precision how much it will cost to meet the MDGs in that country or community.

At the outset, it is important to admit that our knowledge about important aspects of MDG costing equals, at best, our ignorance. The severe limitations associated with any costing methodology must be acknowledged; it must be accepted that ultimately the exact cost of achieving the MDG targets is unknowable. Thus, MDG costing must be addressed with humility, flexibility and from a point of view of learning. The degree of uncertainty about the outcome of existing methodologies cannot be over-emphasised. Five main weaknesses deserve to be highlighted.

First, different approaches, delivery mechanisms and policies exist for reaching the MDGs. Each of them has different unit costs and different cost functions. Generic drugs, for instance, are less expensive than brand-name medicines; home-based care is less costly than institution-based care; day schools are less pricey than boarding schools; community-driven initiatives and grass-roots involvement lower the cost of delivering education, health care and water supply. Some interventions, such as promoting hand-washing, combine high impact with low cost; others are more costly, especially the development and rehabilitation of basic infrastructure.

The cost-effectiveness of specific interventions will depend on the institutional and policy environment in which they occur. Selecting the best delivery mechanism and defining the appropriate policy framework will typically reduce costs. But their optimal choice cannot be known *ex ante*. The notion of ‘good’ policies – which is integral to several approaches to MDG costing – involves judgement and assumes that they are value-free and are applicable across all borders.

Second, most MDG cost estimates use a one-size-fits-all approach, based on fixed coefficients and linear relationships. They seldom allow for economies or diseconomies of scale. Although adjustments are sometimes made for non-linear relationships, there is no sound basis for choosing one specification of non-linearity over another. ‘Average’

unit costs are commonly used but they seldom provide an adequate basis for estimating total costs. The cost of expanding the coverage of a service in health and education by an extra ten percentage points, for instance, will depend on whether the country's coverage moves from 50 to 60 per cent or from 90 to 100 per cent.

Marginal costs are not always better because the determination of the extra cost will depend on the entire cost function. We need to know the cost of all additional units; not just the cost of the next unit. But the cost function as a whole is unobservable.

Neither can a quantitative approach address the qualitative and efficiency aspects of implementing the MDG agenda. Speculations about the nature of the cost function can only undermine the reliability of the results. The problem is likely to grow as cost estimates are projected further into time – making once-and-for-all cost estimates for the next 10 years rather pointless.

In addition, it cannot be assumed that the cost will be unrelated to the scale of operations. A major effort to reach the education target, for example, may increase the demand for trained teachers so as to push their wages upwards – thereby increasing the cost of achieving universal primary education.

Moreover, constant growth elasticities of poverty and fixed incremental capital-output ratios are crude approximations because they change in time and in space. This is not a statistical quirk but reflects real differences across countries in endowments, in histories, in income distribution, in poverty levels and in development trajectories. Any time series confirms that the relationship between economic growth and the level of poverty is highly unstable.

Third, because the MDG targets are inter-related, adding up their individual costs will lead to serious over-estimations of the total cost. In technical terms, this is called 'positive externalities'. The MDGs are also characterised by 'joint production'.

Positive externalities mean that the outputs generated for one target serve as inputs to other targets. Girls' education, for instance, helps to reduce child mortality and HIV infection. Ignoring these important inter-linkages can lead to significant over-estimations of the total MDG cost. The existence of such synergies is beyond dispute; what is a matter of debate is the exact quantification of their cost implications. There is no consensus because the magnitude and character of the externalities themselves are not always clear. For instance, quantifying the cost of addressing gender discrimination, and its impact on all MDG targets, is enormously challenging.

Joint production means that one input simultaneously affects several targets. Nurses, doctors and hospital beds, for instance, help to achieve several MDG targets – such as child and maternal mortality and malaria control. When one input affects several targets at once, then the cost function for a separate MDG target cannot be defined. The cost of achieving the entire set of MDGs cannot be estimated without understanding the manner

in which specific inputs help to advance multiple goals. Since joint production is ubiquitous, it can bias MDG cost estimates in a major way.

Fourth, absorptive capacity will determine the efficiency and effectiveness of reaching the MDGs. When extra money cannot be adequately absorbed, it will lead to greater inefficiencies. However, intangible factors play an important role in determining absorptive capacity. Country-specific campaigns against hunger or for education have shown that absorptive capacity is not fixed – not even in the short-term. In addition, structural reforms and institutional capacity needed to improve management and fight corruption all require extra money. Additional resources can significantly relax absorptive constraints because insufficiencies and inefficiencies are not independent but very much interdependent. Thus, extra resources can be a prerequisite for enhancing absorptive capacity, not the other way round.

Finally, the HIV pandemic and other emergencies – such as conflict – will have an obvious impact on the total cost for achieving the MDGs but it cannot be quantified with any degree of confidence. We know, for example, that achieving universal primary education will cost more when many teachers are HIV-positive. But we have no way of knowing how much more.

In addition to these methodological limitations, data weaknesses often add to the unreliability of MDG cost estimates.

4. Costing without confidence

Given the methodological challenges and data weaknesses, it is not surprising that MDG cost estimates vary greatly – globally, nationally and sectorally. It is particularly difficult to have much confidence in global cost estimates, with existing estimates ranging from an extra \$30 billion per year to over \$100 billion per annum.

Among the many examples that could be used, we highlight the case of Uganda for which several cost estimates exist for achieving universal primary education. UNICEF, UNDP, the World Bank and the UN Millennium Project sponsored such work – with all estimates relating to the early 2000s. Each of the four studies follows a different approach and makes various assumptions about issues such as the pupil-teacher ratio, the proportion of the budget for teaching materials, and the level of teachers' salaries. None of these assumptions appears exaggerated or implausible. Yet, the four studies yield very different unit costs for one year of primary education in Uganda – ranging by a staggering factor of 5:1. When cost estimates for the education target appear so questionable, then we can only wonder how reliable estimates can be for targets whose price tag is more difficult to quantify – and by extension how reliable aggregate cost estimates can possibly be.

This example illustrates that nobody should be gullible to any cost estimate. All estimates must be interpreted with caution and scrutinised carefully; nobody should be subject to irrational exuberance about their precise nature. In our view, there is no robust or 'best' way of costing the MDG targets.

5. Making sense of MDG costing

Despite the many methodological and data-related problems that bedevil the exercise, MDG costing is important and must be pursued. However, we caution against an approach that pretends to give policy-makers, politicians and the public a precise price tag for achieving the MDGs – nationally, globally or sectorally.

In contrast with a technocratic approach, MDG costing must be placed within the ambit of the national political economy, driven by tailored targets for 2015 that are expressed in intermediate targets and actionable propositions that can be achieved within the next 2-3 years. The political economy that underlies MDG costing cannot be addressed through a purely quantitative approach. Cost estimates must be made context-specific – including vis-à-vis the social and political situation – and must be based on strategic choices for prioritising the ways and means of realising the MDG agenda in that specific context. As technical experts seldom agree on the optimal path towards the MDGs, the most reasonable way is to follow a participatory process that is driven by the key stakeholders, supported by technocrats – not supplanted by them.

An excessive focus on getting the numbers right runs the risk of leading to a situation of ‘analysis-paralysis’, whereby the merits of the different costing approaches will forever be challenged and their results heatedly debated or strongly opposed – thereby postponing action in terms of budget restructuring and aid allocations. Since it is better to be broadly right than to be precisely wrong, MDG cost estimates are best seen as orders of magnitude, expressed as a range rather than a single figure.

In making sense of MDG costing, five elements deserve special attention: (i) relative versus absolute costing; (ii) domestic versus external funding; (iii) financing versus costing; (iv) short- and medium-term versus long-term costing; and (v) ownership versus donorship.

5.1 Relative vs. absolute costing

Cost estimates can be derived as either absolute amounts or in relation to national income or the national budget. A relative approach that is used as a rule of thumb and flexible vis-à-vis the level of income, is preferable to the use of a fixed dollar amount. UNESCO’s statistical yearbook, for instance, indicates that absolute expenditure on education ranges widely across countries. When expressed in absolute dollar figures, industrialised countries spend about 40-50 times more per student than low-income countries. But when expressed as a percentage of national income, the range narrows considerably – with most countries spending between 3-6 per cent of national income on education.

Others prefer absolute cost estimates. For instance, it is estimated that public health spending should be at least \$40 per person per year to guarantee basic health care. However, the principal cost item for delivering health care services is labour, whose cost is closely related to the level of economic development of the country. Salaries for nurses

and doctors vary enormously across national borders because they relate to the level of national income. Hence, a fixed dollar amount in health spending will buy considerably more health care in China than in Chile, for example. The same is true for education and other services.

Admittedly, certain cost items can be expressed in absolute terms – such as imported medicines – but they do not justify absolute costing to becoming the norm. Teachers, nurses and doctors are not freely mobile across borders; the cost of their labour cannot be assumed to be uniform. Thus, MDG costing is best driven by relative costing.

It could be argued that any cost estimate can be described either as a relative share or as an absolute amount; but more is at stake than a simple accounting convention. Relative estimates give a better indication of a country's efforts to meet agreed targets than absolute cost estimates do.

5.2 Domestic vs. external funding

More and better aid, as well as steeper debt relief, will be critical for achieving the MDGs, especially – but not exclusively – in the least developed and low-income countries. But as the case is being made for doubling global foreign aid, individual countries are not always given the space for setting more expansionary fiscal policy to accommodate these external resources.

In addition, different disbursement mechanisms are needed to reduce the vulnerability of a country's anti-poverty programme to non-compliance with a variety of conditionalities – which frequently turned them into 'stop-go' programmes in the 1980s and 1990s. Proposals such as 'fixed and variable' tranches are meant to make aid flows less volatile and more predictable.

Several costing exercises assume that most of the funding gap vis-à-vis the MDGs will be covered by foreign aid. We consider that the bulk of the extra investment will need to come from domestic sources – through savings and taxation as well as through private-public partnerships. It would be erroneous to assume that most of the funding gap can be financed from external sources.

This does not diminish the value of foreign aid and debt relief. Since pro-poor policies are never neutral vis-à-vis the country's income distribution, they are bound to meet stiff resistance. For instance, foreign aid can help in easing the resistance to inter- and intra-sectoral reallocations in the national budget, which will be required in most cases for reaching the MDGs.

5.3 Financing vs. costing

Ultimately, the only correct answer to the question of 'How much will the MDGs cost?' is 'more' – albeit that the exact amount cannot be known. Hence, MDG costing must always go hand in hand with MDG financing – examining the potential of various sources of funding, including general taxation, cost recovery for non-basic services, private-public partnerships, foreign aid and debt swaps. A combined financing strategy

that is based on domestic and external resources will give concrete expression to the MDGs as a global deal and as a framework for mutual accountability.

Pro-poor resource generation – a subject that receives scant attention in most poverty reduction strategy papers (PRSPs) – is at the heart of the debate on MDG costing. Most PRSPs now make a stronger case for pro-poor public expenditure – partly as the result of the UN’s advocacy and analytical work on the 20/20 Initiative. While they emphasise the gains in allocative efficiency that stem from expenditure-switching measures, few pay adequate attention to the link between development goals and revenue targets.

During the 1990s, the tax system has been eroded and has become less pro-poor in many countries. But high-performing countries in terms of human development have historically mobilised adequate levels of public revenue. Tax reforms are urgently needed to generate more domestic resources for the MDGs, and to generate them more equitably – a venture that will require a rethinking about setting restrictive fiscal targets and tight inflation targets. Ceilings on public finance have to be set in line with the country-specific targets; short-term fiscal constraints cannot eclipse the long-term MDG vision.

5.4 Short- and medium-term vs. long-term costing

Given the methodological and data weaknesses, it would be ill advised to try to estimate the MDG costs covering the entire period until 2015. It is infinitely more important to estimate the cost implications of the MDGs for the next 2-3 years than to estimate them for the next 10 years. The longer the time horizon, the less reliable such estimates become; each additional year lessens their potential accuracy.

The question of how much the MDGs will cost must be framed within a short-to-medium time horizon, within a 2-3 year rolling framework. The PRSP and the medium-term expenditure framework (MTEF) provide such rolling frameworks. Unfortunately, they are not being used for the purpose of forecasting needs, identifying gaps and mobilising resources. An independent evaluation on the PRSPs [World Bank, 2004] notes, “Many PRSPs have not been reliably costed and fail to provide strategic prioritization” and “The hard choices in prioritizing actions over the short to medium term have not been made in most PRSPs.” The report also concludes, “PRSPs [...] focus largely on leveraging public expenditures to reduce poverty and have not uniformly delineated non-expenditure-related policies or actions [...] such as tax/revenue policies”.

Three practical steps are required to align the national poverty reduction strategy with the MDGs. First, set tailored targets for 2015 and beyond. Second, express them in intermediate targets and actionable propositions for the short- and medium-term so as to generate a stronger political momentum because they will have to be achieved by the current leadership – which is not the case for 2015-targets. Third, estimate the cost of the intermediate targets so they can drive the macro-economic and sectoral policy frameworks as well as the national budget. Steps 2 and 3 are more technical in nature, while step 1 must be driven by a process of political economy.

Intermediate targets and actionable propositions for the next 2-3 years can cover a variety of things, ranging from immunising children to iodising salt, training teachers and building schools and feeder roads, drilling boreholes and planting trees, treating HIV/Aids patients and distributing bed nets, and abolishing user fees for basic social services; as well as improving statistics because they fuel the power of quantification that underpins much of the MDG agenda. Issues of absorptive capacity and Dutch disease need to be addressed too. But flexibility will be key because it cannot be known in advance with any degree of certainty or precision how exactly the MDGs will be achieved in country-specific circumstances.

Setting intermediate targets presupposes that the shape of the trajectory for reaching a particular target by 2015 is known in advance. Frequently, the trajectory is assumed to be linear, but for some targets it can be argued that progress will be fastest in the early years when the so-called low-hanging fruits can be harvested, and that it will slow down as the country gets closer to the target. For other targets, it can be assumed that initial progress will be slow until institutional and human capacities are developed, gender discrimination is addressed and physical infrastructure is in place. The former implies that the trajectory will be logarithmic in nature; the latter indicates that it will be exponential in shape. Ultimately, the exact shape will depend on country-specific and target-specific circumstances. But alternative trajectories must be considered besides the linear one because a straight line seems to be the exception rather than the rule.

5.5 Ownership vs. donorship

Many perceive the attempts to quantify the price tag of the MDGs as driven by external partners, based on central planning of a bygone era. Such perceptions need to be acknowledged because they undermine national ownership. For the targets to trigger real change on the ground, a stronger constituency must be mobilised. Global and long-term cost estimates are unlikely to prompt local actors. Country-specific, intermediate and costed targets are more likely to mobilise people and influence national decision-makers.

The periodic consultations between a developing country and its external partners – either in the form of a Consultative Group or a Roundtable meeting – provide an opportunity for substantive discussions about the content and financing of the national strategy for reducing poverty. However, these meetings often focus narrowly on compliance with rules and conditionalities that stem from donorship rather than debating the strategic choices and policy orientations that reflect national ownership.

A Peer & Partner Review is proposed to make the periodic consultations with external partners less donor-centric and more substantive, focused on ambitious country-specific MDG targets. The current mode whereby a developing country faces a large number of bilateral donors and multilateral institutions is not conducive for an equal exchange and a frank debate about an ambitious anti-poverty programme.

The Peer & Partner Review would involve peer countries and a more select group of partner countries to review the anti-poverty strategy, programmes and financing plans. When Nepal, for instance, meets with its external partners, it could be joined by

representatives from Bangladesh, Cambodia, India, and Sri Lanka; and perhaps from another land-locked country such as Bolivia or Lesotho. A person of distinction could join the consultative process – preferably from civil society organisations. The Peer & Partner Review would help to reduce the extent of donorship and deepen the sense of national ownership by advancing a home-grown poverty reduction strategy geared to meeting ambitious MDG targets.

To turn the Peer & Partner Review into a practical proposition, a number of steps will be required, such as consulting with a few developing countries, bilateral donors and multilateral organisations about important details; initiating the process in a few pilot countries on a voluntary basis; choosing the participating peers and partners; linking the review to similar initiatives (such as NEPAD), based on existing documents such as the PRSP. The challenge is to keep the process light and flexible, supported by a small functional secretariat – possibly composed of the World Bank, DAC and UNDP.

6. Conclusion

In the era of the MDGs, prudence is silver but ambition is golden. Business-as-usual will not turn the noble targets into a practical reality by 2015. For the MDGs' sake, the PRSP and MTEF need to make a quantum leap in scale and in ambition. Yet, making that leap does not necessarily require MDG costing over the entire trajectory till 2015 – summarised in a single dollar figure. While it is not possible to obtain reliable cost estimates for the long-term, MDG costing is essential for aligning the national budget and aid allocations with global development goals. The price tag and the financing plan of the MDG targets can only be ascertained meaningfully within the country's own development plan and national budget within a short-to-medium time horizon.

Relative cost estimates tend to be more relevant than absolute ones. In most cases, domestic resources will be more important, more reliable and more sustainable than foreign aid and debt relief. A financing strategy that combines domestic and external resources will give concrete expression to the MDGs as a global deal, based on the principles of shared responsibility and mutual accountability. The government will renew its efforts at reforming policies and at mobilising domestic revenue and private-public partnerships, while the external partners will increase their support for an ambitious but country-specific MDG agenda.

Finally, MDG costing can enhance the strategic nature of the periodic consultations between a developing country and its external partners. Too often, their emphasis is on compliance with rules and conditionalities rather than on substantive discussions about policies and programmes. A 'Peer & Partner Review' can make such consultations less asymmetric and more substantive. It can help lessen donorship and strengthen national ownership by advancing home-grown pro-poor policies; centred on ambitious intermediate targets that drive the national budget and that take account of absorptive capacities.